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TARION

PROTECTING ONTARIO'S NEW HOME BUYERS

2006 Tarion Warranty Corporation Annual Report

Business Strategy

Vision 2010

Our Strategic Plan to Fulfill Our Mandate

In 2006, Tarion embarked upon Vision 2010, a new five-year strategic plan that is focused on Education, Protection and Automation. Within the framework of these themes, Tarion will continue to add to the core services it provides to consumers and builders, and will also enhance its internal capacity through staff development. Tarion's pursuit of Vision 2010 will help ensure that consumers are protected and informed, that Ontario's new home builders are supported in satisfying today's new home buyers, and that the Corporation is better able to fulfill each area of its statutory mandate.

2006 Strategic Initiatives

Improved Warranty Coverage

- Total warranty protection was increased during the year from $150,000 to $300,000. (See Page 13).
- A Special Committee on Delayed Closings was formed to recommend improvements to regulatory provisions that protect new home buyers from undue delays in the completion of their home (See Page 14).

Expanded Consumer Education

- The number of educational seminars for new home buyers was increased so that Tarion Seminars are now offered in Toronto, Ottawa and London, Ontario. These changes resulted in a 19% increase in total attendance. (See Page 14).

Increased Public Awareness of Tarion

- Tarion's marketing efforts resulted in corporate awareness of 62% among new homeowners and 15% among the general public, representing year-over-year gains of 21% and 9% respectively.

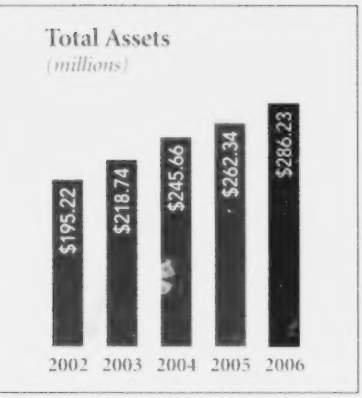
Enhancements to the Tarion Builder Portal

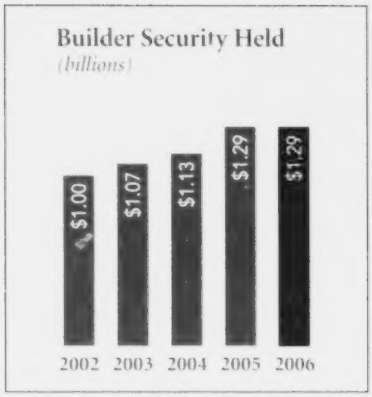
- New functionality was added to the Builder Portal which allows builders to monitor their after-sales service performance, make improvements and compare their results with provincial averages. (See Page 20).

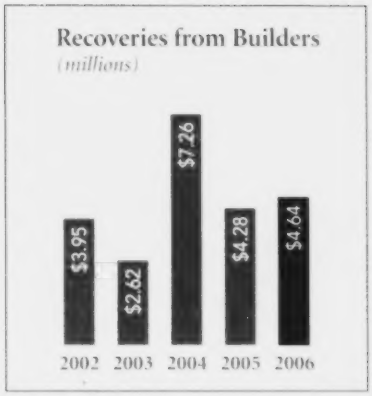
Building a High Performance Organization

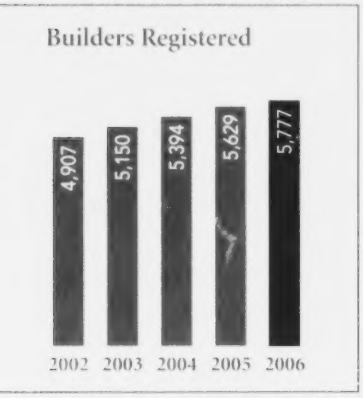
- Throughout the year Tarion employees attended 609 days of management and business skills training.
- All Call Centre and Claims staff attended specialized customer service training courses. (See Page 24).

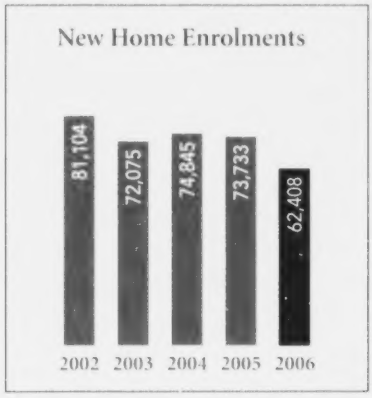
2006 Key Operational Highlights



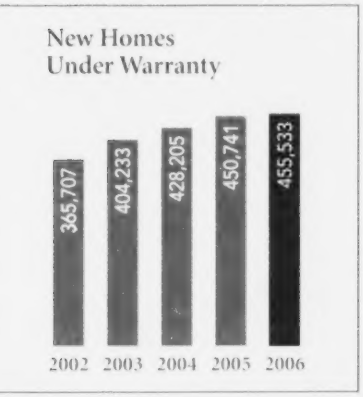


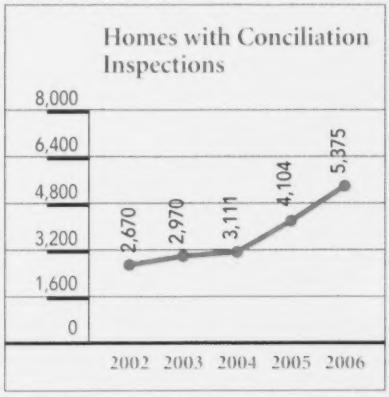


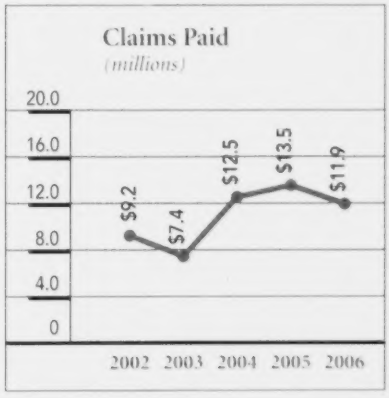




* Warranty Claims Liabilities are estimates of future warranty costs.







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Tarion At-a-Glance

Our Corporate Mandate

2008-02695/

Tarion Warranty Corporation is a private corporation established in 1976 to provide protection for all consumers who purchase a new home or condominium residence in Ontario.

Tarion administers the *Ontario New Home Warranties Plan Act* ("the Act"), on behalf of the Government of Ontario, which requires that builders offer a warranty to each purchaser of a new housing unit in Ontario. Home buyers are protected by one year, two year and seven year warranties that cover defects in workmanship, water penetration and major structural defects as well as delayed closing and deposit protection. The Corporation manages a guarantee fund to ensure that the warranty offered to a consumer will be honoured if the builder refuses to do so, or in the event of builder insolvency. Tarion also establishes and manages minimum time standards for builders to complete after-sales service, and adjudicates issues between homeowners and builders. Currently, there are more than 455,500 homes in Ontario eligible for warranty protection under the Act.

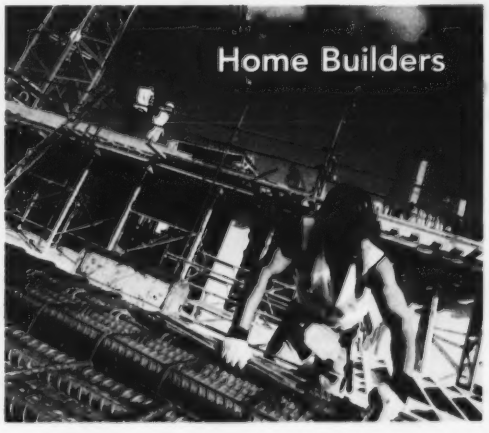
In addition to standing behind the builder's statutory warranty, Tarion acts as the Regulator of the home building industry in Ontario, responsible for the licensing of all new home and condominium builders in the province. Builder licensing occurs annually and it involves the establishment of individual terms and conditions of registration in accordance with the Act. By the close of 2006, the number of registered builders in Ontario was more than 5,700. Tarion is also responsible for enforcement of builders' compliance with the Act. Beyond this regulatory role, the business of the Corporation is similar to a property and casualty insurance company: it takes in fee revenue, establishes reserves and pays out claims.

Tarion's mandate is unique in Canada. No other province or territory transfers responsibility and liability for management of the home building industry to an independent organization. In fulfilling this mandate, the Corporation strives to establish policies and business practices that balance the interests of its stakeholders: new home owners, home builders and the Government of Ontario.

Tarion's customers are derived from two core stakeholder groups:

Tarion protects Ontario's new home buyers and ensures they receive the new home warranty rights they are entitled to by law.

Tarion licenses all new home builders in Ontario and ensures that they comply with the provisions of the statutory warranty.



Responsive to New Home Buyers

243,594

Number of customer calls received by our Contact Centre

1,650

Number of consumers who attended Tarion Educational Seminars in Toronto, Ottawa and London

248,624

Number of visitors who sought information through our website

8,805

Number of consumers and builders who visited our walk-in Customer Centre in Toronto

Supporting Builders

5,777

Number of Ontario new home builders registered with Tarion at year-end

627

Number of builders who attended Tarion's File Review Clinics

50%

Increase in charges laid against illegal builders

1,700

Builders who now use Tarion's Builder Portal, which provides electronic access to Tarion's files

Focusing on Our Stakeholders

Message from the Chairman of the Board

In 2006 Tarion Warranty Corporation celebrated 30 years of protecting Ontario's new home buyers. Just as the times have changed over the past three decades, so too has Tarion made changes that have effectively transformed the Corporation and enabled it to better meet the needs of its major stakeholders: the Province's new home buyers and builders.

The last few years have been a period of particularly rapid transformation at Tarion. With continued implementation of strategic initiatives, Tarion is well positioned to deliver its core services effectively and fulfill all aspects of its corporate mandate.

I am extremely proud to have served as Tarion's Chairman of the Board for the past three years, and to have witnessed first-hand the building of a strong corporate infrastructure throughout the organization. The focus on customer service has led to the development of important new services for both consumers and builders that are being well used. On behalf of the Board, I would like to thank Greg Gee, his management team and all of Tarion's employees for another productive and successful year.

Oversight of Tarion's business objectives is provided by a Board of Directors comprised of representatives from Ontario's new home industry, the provincial government and consumers. 2006 saw the arrival of one new member to the Board, with the nomination during our Annual Meeting on March 28, 2006 of Julie DiLorenzo, President of Diamante Development Corporation. At the meeting, thanks were also given to departing Board member Joe Valela and Associate Member Walter Moodie for their valued service and contributions to Tarion.

As I commence my fourth year as Chairman in 2007, I look forward to continuing to work with Greg Gee and his executive team, as well as with the other members of the Board, and to watching Tarion continuing to evolve as the regulator and consumer protection agency for Ontario's new home building industry.

Robert E. Wade
Chairman of the Board

Message from the President and Chief Executive Officer

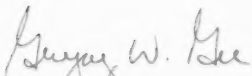
The record number of new homes constructed in Ontario in each of the past four years finally began to slow in 2006. The Corporation enrolled 62,408 new homes during the year, down some 18% over the prior year, but nonetheless, another strong year. The condominium sector accounted for 31% of new enrolments in 2006, representing a substantial change since 2003 when condominium units constituted only 20% of new housing enrolments.

In 2006, our management team renewed its focus on providing exceptional service to our customers. The challenge has been to find new ways to meet customer needs, while working diligently to exceed customer expectations in terms of service delivery. During the year, we doubled warranty coverage on all new homes in Ontario to $300,000, making Tarion the market leader in aggregate warranty coverage in Canada. Following on the success of our retail Customer Centre in Toronto, we opened modern new Customer Centres in both London and Ottawa. We also continued to expand the educational services available to new home buyers and home builders. Attendance at Tarion Consumer Seminars was up 19% for the year, and our File Review Clinics for builders saw an increase in attendance of more than 50% for the year. We also expanded the electronic file information on new homes that we make available to the building industry through our Builder Portal. By using the latest in technology, we have been able to reduce our service costs while providing additional information to builders to enable more timely and efficient after-sales service for new home buyers.

In terms of financial highlights, changes to the management of our investment portfolio led to a restructuring in 2006 which gave rise to nearly $24 million of capital gains. Enrolment fee revenue was lower for the year by about 4% to $33 million. Claims paid were marginally lower than the prior year at $11.9 million, however, claims incurred net of recoveries were substantially lower by more than $8 million for the year, as a result of reduced provisions necessary for new claims. Due largely to capital gains realized from the investment portfolio, the Corporation had excess of revenue over expenses of $30 million for the year, which has further contributed to the very strong financial position of the Corporation.

The true strength of the Tarion organization is its people. I want to acknowledge the significant contribution made by our employees over the past year as we continued to build on our customer service imperative. Considerable time and resources were devoted to training and learning initiatives during the year to ensure that our employees at each level have the skills and knowledge required to serve our customers. This is an ongoing challenge, but strong progress is evident.

I look forward to working with Tarion's Board of Directors, our senior management team, and staff at all levels in the organization in 2007, as we continue in our quest of providing consistent, impartial, high quality, professional services to our customers – the buyers and builders of new homes in Ontario.



Gregory W. Gee
President and Chief Executive Officer

Board of Directors

Left to Right

S. Scott Cameron
President,
Cameron Stephens
Mortgage Capital Ltd.
Toronto

Christopher S. Spiteri
Associate,
Augustine Bater Polowin LLP
Ottawa

Harry Herskowitz
Vice Chair, Partner, DelZotto,
Zorzi, Toronto

Robert E. Wade
Chairman,
(former Mayor of Hamilton)
Hamilton

Tony Campanale
President,
Campanale Homes
Ottawa

Julie DiLorenzo
President,
Diamante Development
Corporation
Toronto

Gregory W. Gee
President &
Chief Executive Officer,
Tarion Warranty Corporation

Left to Right

Robert Cooper
President,
Alterra Group
of Companies
Toronto

Robert G. Dowler
Assistant Deputy Minister,
Policy and Consumer
Protection Services Division,
Ministry of Government
Services

Dick Brouwer
Partner,
Zebro Development Ltd.
London

Victor Fiume
General Manager,
The Durham Group
(OHBA Observer)
Oshawa

Mary Pitt
Corporate Director,
Ottawa

Brian K. Johnston
President,
Monarch Corporation
Toronto

Karen Kinsley
President & CEO,
Canada Mortgage and
Housing Corporation
Ottawa

Peter Saturno
President,
Midhaven Homes
Oshawa

(MISSING FROM PHOTO)
Peter R. Smith President, Andrin Homes Limited, Brampton

Responsibilities of the Committees of the Board

Committee	Members	Key Responsibilities
Executive Committee	**Robert Wade** (Chair) **Dick Brouwer** **Tony Campanale** **Greg Gee** **Harry Herskowitz** **Brian Johnston** **Mary Pitt**	The Executive Committee provides guidance to the full Board on governance matters as well as on policy issues related to government and industry relations. In addition, the Committee deals with executive compensation and management resources matters, the handling of significant claims and policy matters related to the licensing of home builders.
Audit Committee	**Dick Brouwer** (Chair) **Scott Cameron** **Julie DiLorenzo** **Karen Kinsley** **Christopher Spiteri**	The Audit Committee, composed entirely of independent Directors, reviews the annual audited financial statements and financial operating performance, the assessment of reserves and the results of capital adequacy testing. The Committee is responsible for the development and monitoring of policies to address risk management as well as the internal control framework. The Committee also makes recommendations to the Board with respect to the appointment of an external auditor, the external actuary and the pension plan actuary and administrator.
Investment Committee	**Brian Johnston** (Chair) **Scott Cameron** **Robert Cooper** **Peter Smith**	The Investment Committee considers and recommends investment strategies, plans and policies related to the invested assets of the Corporation. The Committee oversees the selection and appointment of one or more investment managers and reviews and approves the investment policies of the Corporation each year. It also reviews reports from fund managers on investment activities and measures investment results against the investment goals of the Corporation. In addition, the Committee is responsible for the management of assets related to the pension plan of the Corporation.
Consumer & Communications Advisory Committee	**Harry Herskowitz** (Chair) **Robert Dowler** **Mary Pitt** **Peter Saturno** **Christopher Spiteri** **J. Richard Blickstead*** **Deborah Brown*** **Martin Redfern*** **Whipple Steinkrauss*** **Chris Ward***	The Consumer & Communications Advisory Committee acts as a forum to provide input to management and the Board on strategic matters with respect to consumer protection initiatives and external communications by Tarion to consumers. The Committee includes members of the Board who represent Tarion's major stakeholders together with external members with expertise in consumer relations and/or the communications and marketing industry. The Committee assists Tarion management with consumer policy development and development of communications strategy by acting as a sounding board to provide insight and input on issues, by making recommendations regarding the development and delivery of consumer protection policies, by analyzing relevant consumer research data and by giving insight into current communication programs and trends.

* Non Board member participant.

Governance Policies

Independence

To ensure independence of the Board and management, an outside Director acts as Chair of the Board. Only one Director, the President & Chief Executive Officer, is a member of Tarion management.

Board Composition

In accordance with the by-laws of the Corporation, the Board of Directors is composed of representatives from a number of the Corporation's stakeholders, each with an interest in the home building industry in Ontario. These include representatives from the Ontario Home Builders' Association (OHBA), members appointed to represent the perspective and interests of Ontario consumers, representatives from areas of the financial industry whose work is relevant to the operations of Tarion and members who have a background with provincial and municipal governments. The Board currently has 15 members and one associate non-voting member.

Financial Controls

The Audit Committee of the Board is composed entirely of outside and unrelated directors whose responsibilities are set forth in a detailed Committee mandate. The Committee has the opportunity to deal directly with the external auditor regarding issues arising from the financial statements, and with the external actuary regarding the claims reserves of the Corporation.

Risk Management

The Board, together with each of the Audit, Investment and Executive Committees, monitors, reviews and approves adherence to corporate policies to manage and control risk, as well as compliance with policies of the Corporation and regulatory requirements.

Strategic Planning

The Board engages in an intensive strategic planning process each year. This takes into account business policy initiatives and opportunities as well as operational and financial risks. Throughout the year, the Board reviews corporate performance against the Company's annual business plan and strategic objectives.

Annual Business Plan

Management prepares an annual Business Plan together with a budget, which are submitted to the Board for approval each year.

Annual Objectives

All employees of the Corporation have written performance objectives each year, and their compensation is determined in part by an evaluation of their performance against these objectives.

Code of Governance Practices

Each member of the Board is required to sign a Code of Governance Practices that has been approved by the Board. This Code is intended to assist the Directors in performing their responsibilities to the Corporation with appropriate discipline and dedication.

Directors' Attendance for 2006

Director	Board of Director Meetings	Committee Meetings
Robert E. Wade	6 of 6	6 of 6
Dick Brouwer	6 of 6	7 of 9
S. Scott Cameron	6 of 6	6 of 6
Tony Campanale	5 of 6	6 of 6
Robert Cooper	6 of 6	3 of 3
Julie DiLorenzo	4 of 4	1 of 2
Robert G. Dowler	5 of 6	1 of 3
Victor Fiume	6 of 6	0 of 0
Gregory W. Gee	6 of 6	15 of 15
Harry Herskowitz	6 of 6	9 of 9
Brian K. Johnston	6 of 6	6 of 6
Karen Kinsley	3 of 6	3 of 3
Mary Pitt	6 of 6	5 of 6
Peter Saturno	6 of 6	3 of 3
Peter R. Smith	5 of 6	3 of 3
Christopher S. Spiteri	6 of 6	3 of 3

Notes on Directors' Attendance:

1. The record of attendance of Directors relates to the Meetings of the Board of Directors and of the Board Committees held by the Corporation during 2006.

2. The number of Board and of Board Committee meetings held by the Corporation during 2006 was as follows:

Board of Directors	6
Executive Committee	6
Audit Committee	3
Investment Committee	3
Consumer & Communications Advisory Committee	3
Total	21

Leadership Team

Left to Right

Bill R. Wallace
Vice President,
Information Systems

Robert S. Jewett
Vice President,
Claims

Robin E. Fitzgerald
Senior Vice
President,
Operations

Robert P. Mitchell
Director, Industry
and Government
Relations

Mike E. Coté
Vice President,
Builder Relations

Eileen M. Holden
Vice President,
Human Resources

Suzanne M. Tiffin
Vice President,
Customer Services

Tim P. Schumacher
Vice President and
General Counsel

Gregory W. Gee
President and Chief
Executive Officer

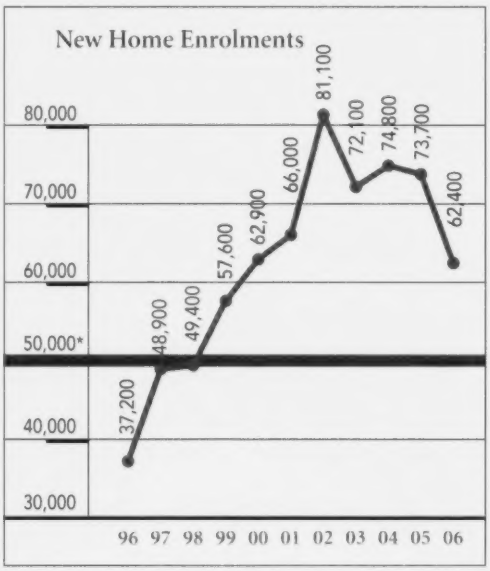
Janice Mandel
Vice President,
Corporate Affairs

John E. Becevello
Vice President
and Chief Financial
Officer

A. Pat Varcoe
Vice President,
Licensing and
Underwriting

Protecting and Serving New Homeowners

The past six years have been characterized by one of the most robust residential construction markets in Ontario history.



* Any year with enrolments above 50,000 units is considered extremely positive.

The continued buoyancy of the marketplace was reflected in Tarion's operational statistics for 2006, in which a total of 62,408 new homes were enrolled with the Corporation during the year. While enrolments are down 18 per cent from the previous year, Ontario continues to have a strong new home marketplace, where any year which exceeds total new home enrolments of 50,000 units is considered to be a strong year. By year-end, the total number of new homes under warranty had reached 455,533, which means that 10 per cent of Ontario's 4.2 million households* are currently eligible for protection under the Tarion's new home warranty program.

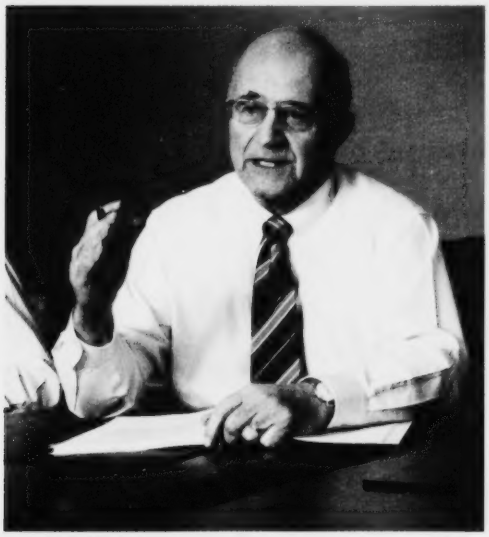
Warranty Protection Doubled in 2006

New home prices also remained strong in 2006, keeping pace with demand. At year-end, the average price for a newly built home in Ontario was $331,710 for a freehold home, $257,140 for a high-rise condominium and $241,799 for a low-rise condominium. To help ensure that warranty coverage remains in tune with market realities, Tarion took a very significant step in 2006 by increasing aggregate warranty coverage from $150,000 to $300,000 for new homes in Ontario with a date of possession on or after July 1, 2006. Due to the financial strength of the Corporation, this additional coverage did not result in an increase in either the home enrolment or registration fees paid to Tarion.

In 2006 Tarion doubled aggregate new home warranty coverage making Tarion the market leader in aggregate warranty coverage in Canada.

* Source: Statistics Canada.

Protecting and Serving New Homeowners



The Honourable Frank Iacobucci, former Justice of the Supreme Court of Canada, chaired a Special Committee that assessed Tarion's Delayed Closing coverage.

Khush Mistry, of Royal Bank, provides information about mortgage options during one of Tarion's New Home Buyer Seminars.

Special Committee on Delayed Closings

On another front, Tarion addressed concerns raised in the media and at Queen's Park about delayed closing protection for consumers. In March 2006, a Special Committee on Delayed Closings was formed by Tarion with former Supreme Court Justice Frank Iacobucci as its Chair. The Special Committee was comprised of 12 members representing a cross section of stakeholders, including freehold and condominium builders of various sizes from across Ontario, land developers, a condominium law expert and consumer representatives. Its mandate was to ensure that there is a modern regulatory framework to protect new home purchasers from undue delays in the completion of a new home, and that they are compensated when delays occur.

Tarion's Board of Directors approved the Special Committee's report in principle at its September 2006 meeting, after which input was sought from stakeholder groups. Included in the report were recommendations reflecting a consensus of the views of the Committee members and a call for an update of the entire delayed closing warranty framework, including administrative rules and procedures. The feedback provided by all stakeholder groups was collected, reviewed and considered by the Special Committee, after which the Report was revised and given final approval by the Tarion Board. Communication and roll-out of new regulations is expected to begin in early 2008.

Educating Consumers

Tarion has long believed that an educated consumer is beneficial to all parties in the statutory warranty process: builders, Tarion and consumers themselves. As such, the organization devotes considerable time and resources to helping new homeowners better understand their rights and responsibilities under the statutory warranty.

One of Tarion's strategic initiatives under Vision 2010 is the expansion of its successful New Home Buyer Seminars, which began in 2004. There are two types of seminars offered to consumers: *Buying a New Home*, which takes purchasers through the new home buying process and provides an overview of the statutory warranty, and *Understanding Warranty Coverage*, which examines the details of the warranty coverage and processes. In 2006, Tarion increased the number of seminars offered, including those held in Mandarin and expanded them geographically. This resulted in a 19 per cent increase in attendance year-over-year and a total of 1,650 consumer participants. All sessions were held at Tarion's Customer Centres in Toronto and Ottawa or at our newest location, London, Ontario.

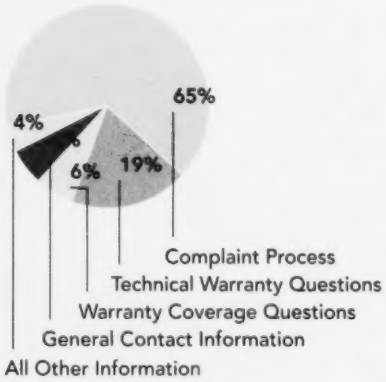
Information about warranty coverage is also available through our corporate website, *tarion.com*, which was accessed by 248,624 visitors in 2006, representing a year-over-year increase of 44 per cent. The most popular areas of our site continue to be the "Find a Builder" section,

The *Construction Performance Guidelines* continue to be one of the most popular areas of Tarion's website.

which provides a snapshot of a builder's track record with Tarion, and the Resources section which offers the opportunity to download warranty-related documents such as the *Construction Performance Guidelines* and the *Homeowner Information Package*, as well as the forms required to make warranty service requests.

Another popular resource is our Toronto-based Contact Centre. Customers have the option of connecting with knowledgeable Tarion staff via e-mail, through our toll-free number, 1-877-9TARION, or customers can visit us in person. In 2006, we received over 243,000 telephone calls from homeowners, builders, and industry professionals looking for information about Tarion or about warranty coverage. Customers calling during business hours reached a live Contact Centre representative 88 per cent of the time. During the year, Contact Centre staff also responded to over 7,700 e-mails and met with 8,800 walk-in visitors at our Customer Centre in Toronto.

Types of Homeowner Calls to Tarion's Contact Centre



Claims Activity

Increased knowledge about the statutory warranty, along with a high level of new home enrolments and the introduction of minimum *Customer Service Standards* in October 2003, are impacting the degree to which homeowners are exercising their warranty rights. In 2006, a total of 60,413 purchasers took possession of a new home enrolled with Tarion, with 45 per cent of them submitting a 30-Day Statutory Warranty Form listing potential warranty items requiring their builder's attention. In most cases, these warranty issues were resolved between the builder and the home buyer without any involvement from Tarion.

Warranty Service Statistics	**2006**	2005	2004
Total New Home Possessions	**60,413**	65,664	69,088
Number of 30-Day Forms Submitted	**26,979**	28,360	25,670
Percentage of Homes for Which 30-Day Forms Were Submitted	**45%**	43%	38%

which provides a snapshot of a builder's track record with Tarion; and the Resources section which offers the opportunity to download warranty-related documents such as the *Construction Performance Guidelines* and the *Homeowner Information Package*, as well as the forms required to make warranty service requests.

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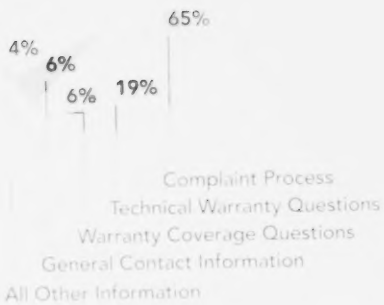
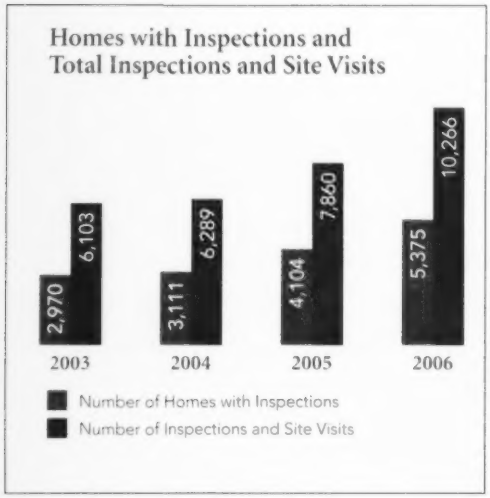


Claims Activity

Increased knowledge about the statutory warranty, along with a high level of new home enrolments and the introduction of minimum *Customer Service Standards* in October 2003, are impacting the degree to which homeowners are exercising their warranty rights. In 2006, a total of 60,413 purchasers took possession of a new home enrolled with Tarion, with 45 per cent of them submitting a 30-Day Statutory Warranty Form listing potential warranty items requiring their builder's attention. In most cases, these warranty issues were resolved between the builder and the home buyer without any involvement from Tarion.

	2006
Total New Home Possessions	60,413
Number of 30-Day Forms Submitted	26,979
Percentage of Homes for Which 30-Day Forms Were Submitted	45%

Protecting and Serving New Homeowners



However, in situations where warranty issues are not resolved, a *Conciliation Inspection* can be requested by the homeowner, in which Tarion will intervene to settle disputes about warrantable items. In 2006, Tarion made 10,266 site visits to freehold homes, condominium units and the common element areas of condominiums (in some cases multiple visits were required). The Claims Department conducted Conciliation or Claim Inspections on 5,375 homes. These figures represent year-over-year increases of 31 per cent in both Homes with Inspections and in Inspections and Site Visits.

The increases can be attributed to an influx of Second Year Statutory Warranty Forms on homes purchased since the *Customer Service Standards* came into effect in 2003, and to a focused effort by the Claims Department on resolving outstanding warranty issues for homes with a date of possession prior to the introduction of this new process.

Total claims paid by Tarion fell by 13 per cent to $11.9 million in 2006, as fewer builder insolvencies occurred during the year. The vast majority of claims – 78 per cent – were related to freehold homes, with condominium units accounting for less than one per cent of claims, and the remaining 21 per cent attributable to condominium common elements.

Claims Paid	**2006**	2005	2004	2003
Number of Claims Paid	**1,189**	1,181	1,165	1,565
Claims Paid ($ millions)				
Freehold Homes	**9.0**	8.8	6.8	5.6
Condominium Units	**0.3**	1.5	1.5	0.9
Condominium Common Elements	**2.6**	3.2	4.2	0.9
Total Claims Paid	**11.9**	13.5	12.5	7.4

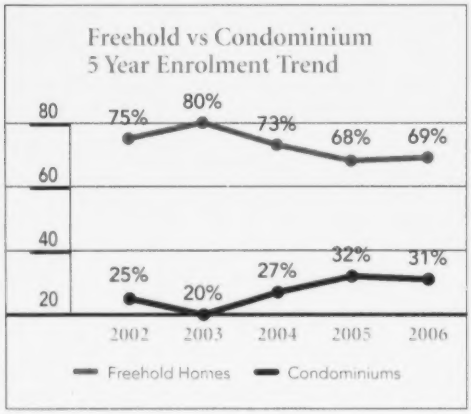
The Appeals Process

The Ontario Licence Appeal Tribunal (LAT) is an informal process for consumers who wish to appeal Tarion decisions concerning compensation claims, and for builders who would like to appeal a decision to refuse a new licence to build new homes in Ontario, or to revoke an existing licence. LAT is an independent tribunal created by the Ontario government to provide an impartial appeals process. In 2006, 214 consumer appeals and 32 builder appeals were filed with LAT from decisions rendered by Tarion, representing year-over-year increases of 66 per cent and 68 per cent respectively. The rise in appeals can be attributed to continuing high volumes of new home enrolments and builder registrations, as well as the Claims Department's effort to resolve warranty issues for homes with a date of possession prior to the introduction of the *Customer Service Standards*. The majority of these appeals were settled by the parties prior to any hearing taking place before the Tribunal.

Supporting Ontario's New Home Builders

Supporting Ontario's New Home Builders

While Ontario's new home marketplace remained strong during 2006, the traditional idea of what constitutes *a home* continued to shift, as an increasing number of consumers opted to purchase a condominium unit rather than a freehold home.



Market Shift to Condominiums Continues

This reality played out in Tarion's operational statistics which show that of the 62,408 new homes enrolled with the Corporation in 2006, 31 per cent were condominium units, whereas as recently as three years ago, condominium units represented only 20 per cent of enrolments. On average, Tarion received 27 new condominium project registrations per month in 2006, and while some of these will not proceed to completion, there are a remarkably high number of projects going to market.

Among the reasons for the rising popularity of condominium living is a growing diversity in the demographics of the new home marketplace, including an increasing number of empty nesters who are choosing condominium living as they downsize. Affordability and the relatively lower price of condominiums is another major factor, particularly in attracting first-time home buyers.

The ongoing health of the marketplace was reflected in the total number of builders registered by Tarion during the year. The number of new home builders continued to rise in 2006 with 5,777 builder registrations, however what is most notable is that over half of the 33 new high-rise builder registrants had previous experience building freehold homes or low-rise condominiums. This is another demonstration of the shift in popularity from freehold homes to condominium units.

Licensing and Underwriting Statistics	**2006**	2005	2004	2003	2002
New Home Enrolments					
Freehold Homes	**43,015**	50,048	54,655	57,680	60,664
Condominiums	**19,393**	23,685	20,190	14,395	20,440
Total	**62,408**	73,733	74,845	72,075	81,104
Builder/Vendor Registrations	**5,777**	5,629	5,394	5,150	4,907
License Refusals/Revocations	**79**	104	56	94	97

Increased Security

In addition to being responsible for licensing all new home builders in Ontario and enrolling new homes, Tarion also obtains security from builders in order to safeguard the Guarantee Fund from which all

Tarion, in collaboration with stakeholders from the building industry, is working toward proactive establishment of guidelines for construction on certain types of soil.

warranty claims are paid. Security is taken in the form of surety bonds, letters of credit, deposit trust agreements, cash held in trust and indemnity agreements. The amount of security required is based on the level of financial risk posed by a particular builder and/or project, with large condominiums typically requiring the most security. Over the last five years, the amount of security held by Tarion has increased by almost 30 per cent, reaching $1.29 billion by year-end 2006.

Builder Security	**2006**	2005	2004	2003	2002
Freehold Homes ($ 000s)	**$ 80,227**	$ 68,635	$ 49,541	$ 41,841	$ 36,256
Condominiums ($ 000s)	**1,210,916**	1,221,651	1,089,352	1,033,446	965,743
Total	**1,291,143**	1,290,286	1,138,893	1,075,287	1,001,999

Research for the Building Industry

In addition to the shift in consumer preference from freehold housing to condominiums, the new home marketplace in Ontario is being transformed by a number of other forces. Chief among these is the decreasing availability of land for new development, a reality that is forcing home builders in some parts of the province to consider construction on what could be potentially problematic types of soil. This practice can result in sizeable claims over the long term, so Tarion has initiated a proactive approach to dealing with the issue.

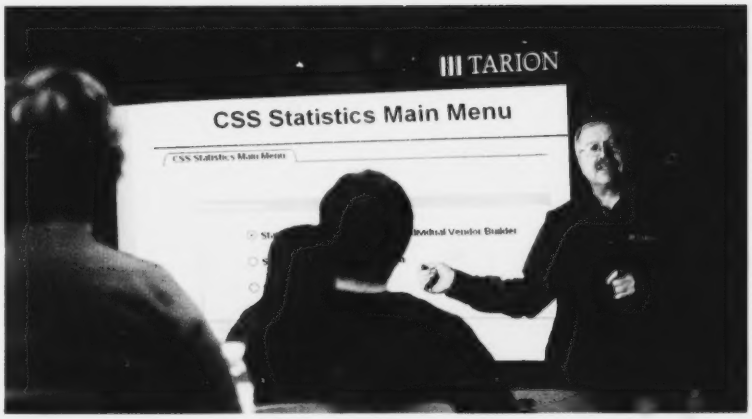
The Corporation acted as the catalyst for bringing together eight builders, their engineers, and the University of Western Ontario's Engineering Department (UWO) to study the risks associated with building residential housing on clay soils in certain parts of the province. The research included extracting soil samples from four builder development sites for analysis by UWO engineers and the subsequent creation of loading predictability models for clay soils.

The result of this study will be shared with builders and the engineering community, with the aim of establishing future best practices and guidelines for constructing on similar soil formations. Tarion will incorporate the knowledge gained from such work into consumer and builder education programs, use it to inform municipalities, Chief Building Officials, and the Ontario Ministry of Municipal Affairs and Housing, as well as use it internally to establish protocols for dealing with major claims issues.

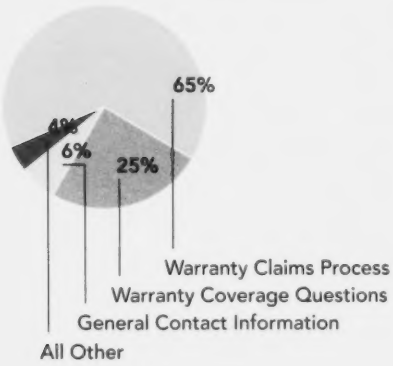
There has been a marked increase in high rise construction over the last several years as a greater number of Ontarians opt for condominium living.

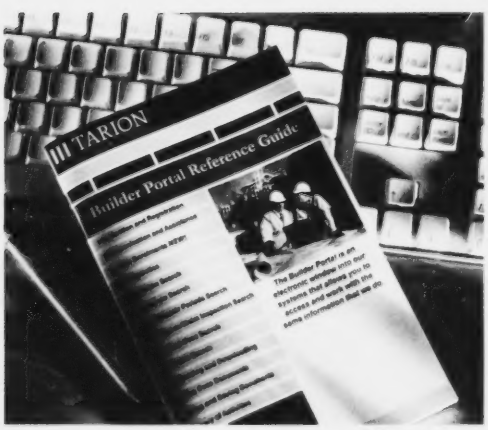
Supporting Ontario's New Home Builders

Mike Coté, Vice-President, Builder Relations provides information to builders about *Customer Service Standards* at one of Tarion's File Review Clinics held throughout the province in 2006.



Frequently Asked Questions at File Review Clinics





Tarion's Builder Portal is currently used by builders that represent more than 80% of new homes built in Ontario, providing them with online access to warranty information to help enhance their customer service delivery.

Portal Helps Builders Improve Customer Service

Ontario's new home builders operate in a highly competitive environment in which consumers are better informed and more demanding than ever. To help builders improve their customer service practices and business efficiency, Tarion provides a number of useful and increasingly popular services.

The Builder Portal stands as one example of a new service from Tarion that gained considerable momentum during the past year. When launched in late 2005, this "electronic window into Tarion" provides builders with secure, online access to statutory warranty information that enables them to address customer service issues immediately.

In 2006, new functionality was added to the Portal which gives builders access to data regarding their own customer service delivery and to compare their results to industry benchmarks. As a result, builders are now able to monitor and evaluate their own performance and make ongoing improvements to meet the standards of the best builders across the province. Tarion's first step toward its Vision 2010 objective of conducting e-business with its customers was also introduced this year with the development of online home enrolment capability. This new feature, which promises to reduce paper-based correspondence for builders, will be rolled out in early 2007.

Since its launch, over 1,700 builders – representing 81 per cent of new homes built in Ontario – have become registered Portal users. In addition, 86 per cent of the top 200 builders in Ontario have discovered how the Portal can enhance key areas of their daily operations, including responsiveness to customer needs.

Builder File Review Clinics Grow in Popularity

Another relatively new Tarion service that grew in popularity during 2006 is our File Review Clinics. These informative sessions provide builders with an opportunity to learn more about Tarion's processes, meet with

Illegal building is a serious problem in Ontario and the province's courts are responding with significant fines.

senior staff, and share ideas and problem solving techniques. New this year were sessions designed to focus on the unique problems and issues associated with condominium construction. In total, 27 File Review Clinics were held across Ontario in 2006, attended by 627 builders from 359 registered companies – up by 143 per cent over the previous year. Clinic locations included Tarion's Toronto, London and Ottawa Customer Centres, and the communities of Guelph, Sudbury, Orillia, St. Catharines, Alliston, Burlington, Waterloo, Barrie and Peterborough.

Builder Relations staff also met individually with 536 builder companies to discuss matters such as after-sales service and to provide other helpful information to assist builders in carrying out their warranty obligations and enhancing the customer service experience for their homeowners.

Illegal Building

An unfortunate reality of Ontario's thriving new home marketplace is that it has attracted individuals that take advantage of purchasers who are unaware of their rights under the *Ontario New Home Warranties Plan Act.* Under the Act, every builder or vendor of a new home sold in Ontario must be licensed by Tarion and must enrol each new home with Tarion prior to its construction.

Tarion's Enforcement Department employs a team of former police officers who investigate illegal building activity across the province. In 2006, the Enforcement team investigated 759 new cases which resulted in 364 charges being laid – an increase of 50 per cent over the previous year's total charges. Provincial courts responded to illegal building activity by handing down 218 convictions during the year, including a five-month jail sentence and fines totalling $100,000 for a repeat illegal builder in Toronto convicted on eight counts of illegal building and furnishing false information.

Tarion also continued its practice of publicizing notable convictions during the year, by distributing press releases to media in local communities where convicted builders operate, and by publishing the names of all convicted builders on *tarion.com*, as well as in our newsletter distributed to builders and government officials. These publicity efforts often result in calls to our enforcement hotline at 1-800-786-6497.

Enforcement Activity	**2006**	2005	2004	2003	2002
New Investigations	**759**	993	961	700	498
Fines Levied ($ 000's)	**674**	817	575	422	203
Charges Laid	**364**	243	993	831	556
Convictions	**218**	287	467	560	324

Supporting Ontario's New Home Builders

AWARDS OF EXCELLENCE
TARION
• 2006 •

Celebrating Builder Excellence

Tarion takes its enforcement role seriously, and it also recognizes the importance of rewarding outstanding builder performance – with a focus on builders who provide exemplary after-sales service to purchasers of new homes.

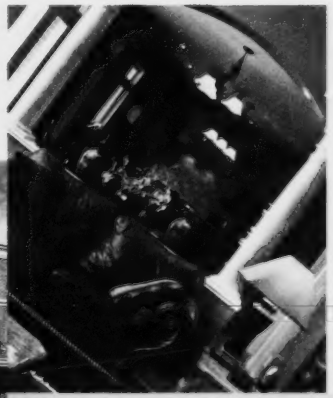
The year 2006 marked the 16th year of the Tarion Awards of Excellence, which is the only home builder awards program in Ontario that focuses exclusively on customer service performance. Awards are given in four categories: Large, Medium and Small Volume Builder of the Year and High-Rise Builder of the Year.

New home builders must meet a set of stringent criteria related to their customer service record with Tarion in order to compete for these Awards. Once builders qualify, the awards process is managed by Decima Research of Toronto, with 70 per cent of each builder's score based on random customer surveys. In addition, builders must provide their customer service philosophy and policies to Decima, with each builder's approach to customer service evaluated for the remaining 30 per cent of the total score. Almost 2,000 homeowners were surveyed for the 2006 Tarion Awards.

2006 Tarion Award of Excellence Winners

< **Great Gulf Homes**, Toronto
High-Rise Category

^
Tribute Communities, Toronto
Large Volume Category



< **Rinaldi Homes**
St. Catharines
Medium Volume Category

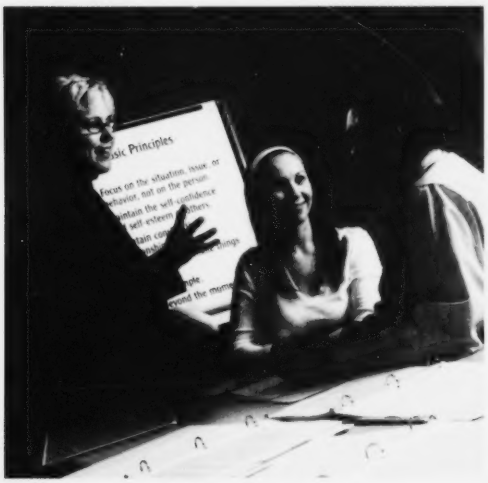
Krepstakies
Custom Home Building
Waterloo Region
Small Volume Category
v

Ensuring Our Strength Continues

Connie Carreiro
Underwriting Analyst
Licensing and Underwriting
Winner / 2006 Ralph Lewis Award

Ensuring Our Strength Continues

Like any organization with a strong customer service focus, Tarion must continually evolve to address changing customer needs and marketplace trends. During 2006, our commitment to ongoing improvement involved building internal capacity to better deliver on our core services, and to further develop the long-term potential of our staff.



In 2006, the vast majority of Tarion employees took advantage of training opportunities to upgrade their skills and increase their capabilities in fulfilling their career goals.

Investing in Our Most Important Resource

One of the key priorities at Tarion is to offer continuous learning that provides our staff with opportunity to build on their existing knowledge base and learn new skills. Doing so enables employees to advance their own careers and helps the Corporation ensure that our staff have the skills and knowledge required to achieve our customer service and job performance standards, and to implement new strategic initiatives in our Vision 2010 objectives.

Staff from all levels of the organization were part of this strategic approach to training, with courses held in-house or provided through external suppliers. Topics included business skills and management training, leadership, service excellence, work-load management, business communication, project management, conflict management and problem solving.

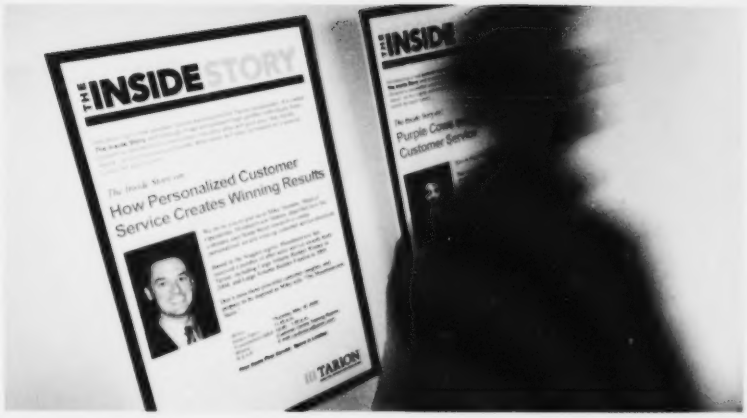
Training was also provided to help staff build their technical skills. For example, to assist our Call Centre Representatives in becoming more proficient at handling customer enquiries by telephone, new training software – called Sivox – was acquired. It provides interactive simulation of typical client calls along with a data screen entry component. Staff use Sivox to practice specific scripts and phrasing that match customer needs, refine their tone of voice and use of language, increase their productivity and call consistency, and boost their data entry proficiency on Tarion's automated systems.

As well, staff in our Claims Department participated in a case-based Scoping and Estimating course during the year. This was conducted by the professional training division of CGI Insurance Business Solutions and was designed to give participants the technical tools to bring greater consistency to the pricing of construction defect claims.

Employee Speaker Series Launched

In order for Tarion employees to effectively carry out their jobs, it is important that they have a thorough understanding of all aspects of the residential construction industry. To help foster such understanding, management introduced a lunchtime speaker series called *The Inside Story* during 2006, in which high-profile industry leaders are invited to talk to staff about home building industry issues and trends – including innovative approaches to providing customer service. Speakers included Stephen Dupuis, Chief Executive Officer of the Greater Toronto Home Builders' Association – Urban Development Institute; Mike Memme, Head of Operations for Mountainview Homes, an award-winning builder from St. Catharines; Hugh Heron, President of Heathwood and Heron Homes, former Chairman of the Corporation; and Danielle Feidler, Vice President of Customer Care at Tridel Corporation, another award-winning builder. The series has proved to be very popular – every session has attracted a standing room only crowd of employees – and plans are to continue this program in 2007.

A new lunch-time speaker series called *The Inside Story* offers Tarion employees the opportunity to hear from high-profile leaders in the residential construction industry.



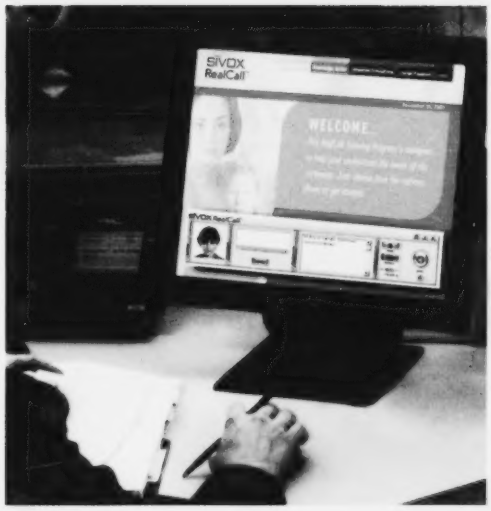
Using Technology to Better Serve Our Customers

The efficient processing of large volumes of data underlies Tarion's ability to meet many of the service-related needs of new homeowners and builders. This is particularly the case when it comes to the administration of our claims function, which requires highly accurate record keeping and quick retrieval of information related to the minimum *Customer Service Standards.*

In 2006, staff in our Contact Centre processed over 235,000 documents including Pre-Delivery Inspection Forms, Statutory Warranty Forms, Agreements of Purchase and Sale, and Certificates of Completion and Possession. This information is available on a comprehensive electronic database that can be accessed by Tarion staff throughout Ontario to manage homeowner claims in a responsive and efficient manner.

To ensure that such claims administration and other key business functions are available, even in the event of some type of disaster, Tarion implemented a Business Continuity Plan in 2006, providing both the protocol and backup facilities for keeping mission critical operations up-and-going. Included in the plan is a step-by-step process that covers all necessary and appropriate actions required to relocate staff and technology to an offsite data facility designed for extraordinary situations.

Successful testing and simulations conducted during the year showed that critical data can be recovered within 48 hours of an emergency. Important organizational processes such as the functioning of the Contact Centre and claims processing can also now be re-established within the same 48-hour window.



With the help of an interactive training tool, Call Centre staff improved their customer service skills.

A Sound Financial Position

A hallmark of the strength of Tarion Warranty Corporation is the fiscally prudent manner in which it handles its financial resources. By applying a long-term growth strategy in managing its investment portfolio, and through a capital management framework using key principles from the property and casualty insurance industry, Tarion is well positioned to weather economic peaks and valleys, thus ensuring that Ontario's new homeowners will continue to enjoy comprehensive warranty protection – now and in the future.

Financial Commentary

Auditors' Report

Actuary's Report

Management's Responsibility for Financial Reporting

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Statement of Surplus

Statement of Cash Flows

Notes to Financial Statements

Financial Commentary

The housing market remained strong in 2006, however housing unit enrolment levels reduced somewhat from 2005 levels. This caused the enrolment fees earned during the year to decrease by 3.8% over the prior year to $33 million.

Overall investment results for the year were up dramatically from the prior year due to realized gains arising from a restructuring of the investment portfolio following the appointment of a new investment manager. The management of the investment portfolio was previously outsourced to one investment management company. As part of the Corporation's continued risk mitigation program, a second management company was retained to manage one half of the portfolio. Also contributing to the high level of investment gains was the increase in trading activity in the summer months as a result of the two managers responding to the volatile market conditions at the time. Overall these activities triggered more than $24 million of capital gains as shown in the Statement of Operations.

Net claims incurred were unusually low for the year. Claims paid remained at a relatively high level; $11.9 million was paid out in 2006, nearly 20% higher than the average of the previous five years. However, while total recoveries were similar to the prior year, provisions for new claims and changes to existing claims provisions were much lower decreasing from $12.2 million in 2005 to $3.8 million in 2006. Several significant claims provisions were decreased in response to a relatively quiet 2006 claims experience.

During the year, the Corporation conducted a thorough review of claims on homes with possession dates prior to October 1, 2003, the start date of the new *Customer Service Standards*, and made significant progress on a formal review of the existing delayed closing policies.

The Corporation added more than $30 million to its surplus for the year due to unusually high investment gains combined with a low level of net claims incurred. The substantial excess of revenue over expenses for the year has further added to the Corporation's financial strength. Based on the Corporation's capital management framework, the total surplus of the Corporation as at December 31, 2006 has been determined to be sufficient. The capital management framework, adopted in 2005, assesses the long term financial strength of the Corporation. The Corporation's capital management program is modeled after the framework used in the P&C insurance industry and was modified to reflect the Corporation's circumstances, including its inability to raise capital in traditional ways. The framework incorporates the business requirements for sufficient capital throughout the economic cycles of the new home building industry, including possible losses from a future catastrophic event.

Auditors' Report

To the Directors of Tarion Warranty Corporation

We have audited the balance sheet of Tarion Warranty Corporation (the "Corporation") as at December 31, 2006 and the statements of operations, of surplus and of cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

Deloitte & Touche LLP

Deloitte & Touche LLP
Chartered Accountants
Licensed Public Accountants

Toronto, Ontario
February 27, 2007

Actuary's Report

To the Directors of Tarion Warranty Corporation

I have reviewed the warranty liabilities of Tarion Warranty Corporation for its Balance Sheet as at December 31, 2006 and their change in the Statement of Operations for the year then ended in accordance with accepted actuarial practice, including the selection of appropriate assumptions and methods.

In my opinion, the amount of these warranty liabilities makes appropriate provision for all warranty obligations, and the financial statements fairly present the results of the review.

Jim Christie

James K. Christie
Fellow, Canadian Institute of Actuaries

Toronto, Ontario
February 27, 2007

Management's Responsibility for Financial Reporting

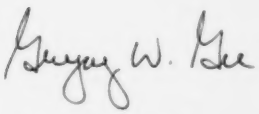
Management is responsible for the integrity of the financial statements and operational information presented in this Annual Report. The financial statements have been presented in accordance with appropriate and generally accepted accounting principles and reflect management's best estimates and judgments. Financial information presented elsewhere in the Annual Report is consistent with these financial statements.

Management maintains a system of internal controls, to provide reasonable assurance that all assets are safeguarded and to facilitate the preparation of relevant, reliable and timely financial information.

The external actuary appointed by the Audit Committee is responsible for ensuring that the assumptions and methods used in the determination of the warranty liabilities are in accordance with accepted actuarial practice, applicable legislation, and associated regulations and directives.

External auditors have examined and reported on the financial statements.

The Audit Committee, consisting of non-executive directors, has reviewed these financial statements with management and the external auditors, and has reported to the Board of Directors, which has approved the financial statements.



Gregory W. Gee
President & Chief Executive Officer
February 27, 2007

John Becevello
Vice President & Chief Financial Officer
February 27, 2007

Balance Sheet

December 31, 2006 ($ thousands)	2006	2005
Assets		
Cash (Overdraft)	**$ 400**	$ (1,071)
Investments (Notes 4 and 7)	**274,552**	251,205
Accrued interest, dividends and accounts receivable	**2,291**	2,664
Capital assets (Note 5)	**6,136**	7,321
Amounts recoverable from builders	**2,319**	1,766
Prepaid expenses and other assets	**529**	459
	$ 286,227	$ 262,344
Liabilities		
Warranty liabilities (Note 6)	**$ 135,962**	$ 144,551
Funds held as security (Note 7)	**37,001**	34,975
Accounts payable and accrued liabilities (Note 5)	**7,261**	7,635
Employee future benefits liabilities (Note 8)	**1,336**	540
	181,560	187,701
Surplus (Note 3)		
Appropriated surplus	**44,000**	40,000
General surplus	**60,667**	34,643
	104,667	74,643
	$ 286,227	$ 262,344

Approved by the Board

Robert E. Wade
Director and Chair of the Board

Dick Brouwer
Director and Chair of the Audit Committee

Statement of Operations

Year ended December 31, 2006 ($ thousands)	2006	2005
Revenue		
Home enrolment fees earned	**$ 33,037**	$ 34,337
Builders' registration and renewal fees	**1,985**	1,989
Investment results		
Interest and dividends	**11,757**	10,369
Net gain on sale of investments	**24,385**	3,402
Investment management fees	**(739)**	(527)
Other revenue	**220**	387
	70,645	49,957
Expenses		
Net claims incurred (recovered) (Note 6)	**$ (817)**	$ 7,920
Salaries and benefits	**22,627**	19,455
General and administrative	**15,430**	13,612
Depreciation and amortization	**3,381**	3,234
	40,621	44,221
Excess of Revenue Over Expenses for the Year	**$ 30,024**	$ 5,736

Statement of Surplus

Year ended December 31, 2006 ($ thousands)	Appropriated		General		Total	
	2006	2005	**2006**	2005	**2006**	2005
Surplus, beginning of year	**$ 40,000**	$ 50,000	**$ 34,643**	$ 18,907	**$ 74,643**	$ 68,907
Change in appropriation (Note 3)	**4,000**	(10,000)	**(4,000)**	10,000	**–**	–
Excess of revenue over expenses for the year	**–**	–	**30,024**	5,736	**30,024**	5,736
Surplus, end of year	**$ 44,000**	$ 40,000	**$ 60,667**	$ 34,643	**$ 104,667**	$ 74,643

Statement of Cash Flows

Year ended December 31, 2006 ($ thousands)	2006	2005
Net Inflows (Outflows) of Cash Related to the Following Activities		
Operating		
Excess of revenue over expenses for the year	**$ 30,024**	$ 5,736
Add (deduct) non-cash items		
Amortization of bond premiums and discounts	**(165)**	1,389
Net gain on sale of investments	**(24,385)**	(3,402)
Depreciation and amortization	**3,381**	3,234
	8,855	6,957
Changes in non-cash balances related to operations		
Decrease in accrued interest, dividends and accounts receivable	**373**	659
Increase in prepaid expenses and other assets	**(70)**	(62)
(Increase) decrease in amounts recoverable from builders	**(553)**	1,398
(Decrease) increase in warranty liabilities	**(8,589)**	1,552
Increase in funds held as security	**2,026**	10,432
Decrease in accounts payable and accrued liabilities	**(374)**	(888)
Increase (decrease) in employee future benefits liabilities	**796**	(149)
Cash provided by operating activities	**2,464**	19,899
Investing		
Proceeds from sale and maturity of investments	**270,952**	65,517
Purchase of investments	**(269,749)**	(84,560)
Purchase of capital assets	**(2,196)**	(2,031)
Cash used in investing activities	**(993)**	(21,074)
Net Increase (Decrease) In Cash During the Year	**1,471**	(1,175)
Cash (Overdraft), Beginning of Year	**(1,071)**	104
Cash (Overdraft), End of Year	**$ 400**	$ (1,071)

Notes to Financial Statements

December 31, 2006 ($ thousands)

Note 1 Corporation Operations

Tarion Warranty Corporation (the "Corporation") was designated in 1976 by the Government of Ontario to administer the *Ontario New Home Warranties Plan Act* (the "Act"). The objectives of the Act include consumer protection, builder regulation and providing consumers and builders with a broad range of services including information and education. The Corporation collects home enrolment and builder registration fees and invests available funds for the purposes of settling warranty claims from homeowners, and providing for investigation, enforcement, and other administrative costs related to its responsibilities in administering the Act. Warranty protection is outlined in the Act and includes providing a warranty to purchasers of new homes in respect of:

- loss of deposit if a builder cannot or will not complete the sale of a home, through no fault of the home buyer;
- specified construction and contractual warranties for defects in work or material; and
- protection against delayed closing, under certain circumstances.

As a non-profit organization, the Corporation is exempt from income taxes.

Note 2 Summary of Significant Accounting Policies

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). In addition, although not required, the Corporation adopts certain accounting requirements of the Office of the Superintendent of Financial Institutions Canada ("OSFI") for property and casualty ("P&C") insurance companies in Canada. These accounting requirements are in accordance with GAAP.

The preparation of financial statements, in conformity with GAAP, requires management to make assumptions and estimates that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities as at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting periods. Actual amounts could differ from those estimates. The most significant estimation processes are related to the determination of warranty liabilities.

Revenue recognition

Home enrolment fees are remitted by builders during the year. These fees, net of refunds, are deferred and taken into revenue as earned, as determined by actuarial calculation, over the warranty period. The deferred portion of home enrolment fees is included in warranty liabilities. If claims experience indicates that home enrolment fees collected will not be sufficient to discharge related liabilities, a provision for premium deficiency is included in the warranty liabilities.

Builders' registration fees are recorded as revenue upon registration and renewal fees are recorded as revenue in the year in which they are due.

Warranty liabilities

The warranty liabilities include deferred home enrolment fees and warranty claim liabilities. Deferred home enrolment fees represent the unearned portion of home enrolment fees remitted by builders. Warranty claims liabilities are estimates of future warranty costs and include estimates of costs for claims reported and in process, and provisions for claims incurred but not yet reported as at the balance sheet date where it is anticipated that costs will be incurred by the Corporation.

Notes to Financial Statements

December 31, 2006 ($ thousands)

The warranty period spans seven years and accordingly, significant periods of time can elapse between the incurrence of claims liabilities and their payment. Accordingly, the estimation of the liabilities involves significant measurement uncertainty.

The liabilities are discounted to reflect the investment income expected to be earned over the period between the incurrence and settlement of claims. Provisions for adverse deviation are added to allow for the inherent measurement uncertainty that arises because actual investment yields may differ from the discount rate; because the actual settlements may occur at amounts that differ from expected settlement amounts; and because the timing of settlements may differ from expected timing.

Claims incurred include claims recoveries and changes in the provisions for claims reported and in process and for claims incurred but not yet reported.

Claims recoveries include amounts recovered from builders on claims incurred during the current year or in previous years and changes in the estimate of amounts recoverable from builders on outstanding warranty claims liabilities. Estimated amounts recoverable from builders are presented on the balance sheet as an asset of the Corporation.

Investments

Certificates of deposit with financial institutions, treasury bills and bankers' acceptances are recorded at cost.

Bonds are recorded at amortized cost. Discounts or premiums on purchase are amortized using the effective interest method over the term of the investment.

Common shares are recorded at cost.

When a decline in the value of an investment is considered other than temporary, a provision for loss is recorded to reduce the recorded amount to net realizable value with the amount of the reduction charged to operations.

Capital assets

Capital assets are recorded at cost less accumulated depreciation and amortization. Depreciation and amortization are provided at the following rates and bases:

Software and applications	–	straight-line over three years
Computer equipment	–	straight-line over four years
Computer equipment acquired under capital lease	–	straight-line over four years or the term of lease if shorter than four years
Furniture and office equipment	–	20% declining balance
Leasehold improvements	–	straight-line over the term of the lease

Employee future benefits

The Corporation accrues its obligations under employee benefit plans and the related costs, net of plan assets. The cost of pensions and other post-employment benefits earned by employees is actuarially determined using the projected benefit method pro-rated on service and management's best estimates of expected plan investment performance, salary escalation, retirement ages of employees and expected health care costs. For the purpose of calculating the expected return on plan assets, those assets are valued at fair value. Past service costs from plan amendments are amortized on a straight-line basis over the average remaining service periods of eligible employees active at the date of amendment.

Note 3 Surplus

The Corporation has adopted a capital management framework modeled after the framework used in the P&C insurance industry, modified to reflect the Corporation's circumstances including its inability to raise capital in traditional ways. This framework incorporates the business requirements for sufficient capital throughout the variations of the new home building cycle, including possible losses from a future catastrophic event. It also reflects the relatively high risk profile of the Corporation's warranty operations, including the high level of measurement uncertainty inherent in its warranty liabilities due to the long warranty period of up to seven years and to other factors explained in Note 6.

In applying the framework, the Corporation has adjusted the amount designated as appropriated surplus to be the amount needed to meet the minimum capital test the federal insurance regulator uses for P&C insurance companies plus an estimate of the amount needed to cover two years of adverse business results. Based on the capital management framework, the surplus of the Corporation as at December 31, 2006 has been determined to be sufficient to cover possible losses from a future catastrophic event as determined by the annual dynamic capital adequacy testing performed during the year.

Note 4 Investments

The following tables illustrate the Corporation's investment portfolio as at December 31:

	2006		2005	
	Carrying Value	**Fair Value**	Carrying Value	Fair Value
Securities with interest rate exposure:				
Bonds issued by federal and provincial governments	**$ 113,176**	**$ 116,528**	$ 104,215	$ 112,278
Financial institution bonds	**38,002**	**39,544**	49,857	51,961
Other corporate bonds	**55,292**	**56,007**	33,197	34,426
Treasury bills	**8,906**	**8,953**	8,225	8,248
	215,376	**221,032**	195,494	206,913
Equity investments:				
Common shares	**59,176**	**91,927**	55,711	96,974
	$ 274,552	**$ 312,959**	$ 251,205	$ 303,887

Notes to Financial Statements

December 31, 2006 ($ thousands)

	2006			2005		
	Unrealized Gains	**Unrealized Losses**	**Net Unrealized Gains (Losses)**	Unrealized Gains	Unrealized Losses	Net Unrealized Gains (Losses)
Bonds issued by federal and provincial governments	**$ 3,929**	**$ (576)**	**$ 3,353**	$ 8,080	$ (17)	$ 8,063
Financial institution bonds	**1,658**	**(117)**	**1,541**	2,283	(179)	2,104
Other corporate bonds	**748**	**(33)**	**715**	1,229	–	1,229
Treasury bills	**47**	**–**	**47**	32	(9)	23
Common shares	**33,080**	**(329)**	**32,751**	43,370	(2,107)	41,263
	$ 39,462	**$ (1,055)**	**$ 38,407**	$ 54,994	$ (2,312)	$ 52,682

Management does not consider the unrealized losses on common shares in 2006 to be other-than-temporarily impaired at December 31, 2006. The unrealized losses on common shares in 2005 primarily consisted of foreign exchange losses.

(a) Securities with interest rate exposure

As at December 31, the scheduled maturities and fair values for securities having interest rate risk exposure are as follows:

	2006			2005		
	Effective Rate (%)	**Carrying Value**	**Fair Value**	Effective Rate (%)	Carrying Value	Fair Value
Term to maturity:[1]						
Due within one year	**4.13**	**$ 12,205**	**$ 12,248**	3.16	$ 8,225	$ 8,248
Due one year through five years	**5.28**	**51,902**	**52,607**	5.10	76,917	78,786
Due five years through ten years	**5.39**	**89,505**	**92,082**	6.08	76,558	81,400
Due ten years through twenty years	**5.38**	**37,165**	**38,482**	6.23	25,798	29,279
Due after twenty years	**4.98**	**24,599**	**25,613**	7.21	7,996	9,200
	5.25	**$ 215,376**	**$ 221,032**	5.64	$ 195,494	$ 206,913

(1) Actual maturities may differ from contractual maturities shown above, since borrowers may have the right to prepay obligations with or without prepayment penalties.

Fair values presented in the preceding tables are based on market values and will vary with interest rate changes.

The Corporation has adopted an investment policy that requires minimum credit ratings of "A" for debt securities at the time an investment is purchased and that limits the concentration in any one investee or related group of investees, except for financial instruments issued by the Government of Canada for which there is no limit. This investment policy is subject to annual review by the Investment Committee of the Board of Directors of the Corporation.

(b) Equity investments

The fair values of common shares are based on quoted market prices or dealer quotes.

(c) Foreign currency exposure

The Corporation regularly monitors its risk associated with foreign currency exposure by reviewing the amount of U.S. dollar denominated investments. As at December 31, 2006, the Corporation had approximately 11.3% (2005 – 26.5%) of the carrying value of equity investments denominated in U.S. dollars and approximately 0.5% of securities with interest rate exposure (2005 – 0.2%).

Note 5 Capital Assets

	2006			2005
	Cost	Accumulated Depreciation/ Amortization	Net Book Value	Net Book Value
Software and applications	$ 7,455	$ 5,321	$ 2,134	$ 2,772
Computer and office equipment under capital lease	3,259	2,211	1,048	1,637
Leasehold improvements	2,288	487	1,801	1,613
Computer equipment	1,128	649	479	687
Furniture and office equipment	1,123	449	674	612
	$ 15,253	$ 9,117	$ 6,136	$ 7,321

The balance of the capital lease obligations arising from the acquisition of certain computer and office equipment was $1,084 at December 31, 2006 (2005 – $1,682). This obligation is reported on the balance sheet in accounts payable and accrued liabilities. The Corporation incurred interest expense of $166 during 2006 (2005 – $124) on the capital leases which is reported in general and administrative expenses on the statement of operations.

Note 6 Warranty Liabilities

The determination of the Corporation's warranty liabilities, which include deferred home enrolment fees and warranty claim liabilities, is dependent on the Corporation's claims handling practices, on actuarial assessments, on the judgment of its management, on historical precedents and trends, on prevailing legal, economic, social and regulatory environments and on expectations of future development. Periodic studies are performed by management and reviewed by external actuarial consultants to assess the adequacy of the warranty claims liabilities recorded for homes and condominiums, as well as the adequacy of deferred home enrolment fees to cover future claims and related administration costs to administer claims.

Notes to Financial Statements

December 31, 2006 ($ thousands)

In general, the longer time period between the incidence of loss and settlement of the related claim, the greater the potential for actual settlement amounts to differ from the recorded estimates. Actual settlements may also differ significantly from the estimates of these liabilities due to the measurement uncertainty involved in establishing assumptions for such variables as future rates of claim frequency, severity, inflation, the ability of builders to fulfill their obligations to home buyers, recoveries from builders and administrative costs.

The following table summarizes the components of the warranty liabilities as at December 31:

	2006	2005
Deferred home enrolment fees, beginning of year	**$ 88,592**	$ 85,726
Fees received	**32,560**	37,203
Fees earned	**(33,037)**	(34,337)
Deferred home enrolment fees, end of year	**88,115**	88,592
Warranty claims liabilities, beginning of year	**55,959**	57,273
Provisions for claims, net of reversals	**3,820**	12,197
Claims paid	**(11,932)**	(13,511)
Warranty claims liabilities, end of year	**47,847**	55,959
Warranty liabilities, end of year	**$ 135,962**	$ 144,551

The following table summarizes the components of claims incurred presented in the statement of operations:

	2006	2005
Provisions for claims, net of reversals	**$ 3,820**	$ 12,197
Less recoveries	**(4,637)**	(4,277)
Net claims incurred (recovered) for the year	**$ (817)**	$ 7,920

Note 7 Funds Held as Security

The Corporation receives security deposits from builders, in the form of cash, letters of credit or other guarantees, on registration of certain projects in order to reduce the risk of financial loss related to future warranty claims from homeowners. Security deposits that are not used to pay claims are either paid back to the builder, or the letters of credit or other guarantees are released, when the Corporation's requirements are met.

Security deposits received in cash are invested as part of the Corporation's investment portfolio. The Funds held as security presented on the balance sheet as a liability are the potentially refundable security deposits received in cash, including cumulative accrued interest thereon of $1,685 (2005 – $1,015). Letters of credit and other guarantees are recognized in the financial statements only to the extent they are expected to be drawn upon to settle known claims. Such amounts are included in amounts recoverable from builders.

During the year, the Corporation incurred interest of $1,173 (2005 – $672) on cash security deposits.

Note 8 Employee Future Benefit Plans

On September 9, 1999 the Corporation's defined benefit pension plan and money purchase pension plan were merged into a new pension plan called The Pension Plan for Employees of the Tarion Warranty Corporation (the "Pension Plan"). The Pension Plan is open to all full-time employees of the Corporation, subject to meeting certain eligibility conditions. Under the terms of the Pension Plan, employees contribute a percentage of eligible employee earnings per year. The Corporation makes contributions for each contributing employee in amounts that vary dependent upon the employee's age and the number of years of eligible service. In addition, the Corporation provides other post-employment benefits ("OPEB"), primarily under various health and dental coverages, on an unfunded basis.

As at December 31, 2006, the fair value of the pension fund assets is $12,323 (2005 – $11,693), which is slightly below the actuarial present value of accrued pension benefits for the Pension Plan estimated to be $12,658 (2005 – $11,581). The accrued pension liability is $761 (2005 – $140).

The accrued benefit liability for OPEB at December 31, 2006 is $575 (2005 – $400).

Key information is as follows:

Actuarial assumptions for pension expense estimates	
Return on assets	6.75%, net of expenses (2005 – 6.75%)
General inflation	3.0% (2005 – 3.0%)
Liability discount rate	5.0% (2005 – 5.75%)
Salary increases	4.0% (2005 – 4.0%)
Mortality	Uninsured Pensioners Mortality Table – 1994
Actuarial assumptions for OPEB expenses estimates	
Discount rate	5.0% (2005 – 5.75%)
General inflation	3.0% (2005 – 3.0%)
Dental care trend rate	4.0% (2005 – 4.0%)
Extended health care trend rate	10.0% (2005 – 10.0%); decreasing by 1.0% annually, commencing in 2008, to an ultimate rate of 5.0%
Mortality	Uninsured Pensioners Mortality Table – 1994
Pension Plan asset mix	
Canadian equity securities	23.0% (2005 – 25.0%)
International and U.S. equity securities	37.0% (2005 – 32.0%)
Bonds	25.0% (2005 – 36.0%)
Cash	15.0% (2005 – 7.0%)

Notes to Financial Statements

December 31, 2006 ($ thousands)

The Corporation has a December 31 measurement date. A valuation of the accrued pension benefit obligation was performed as at January 1, 2005. To estimate the obligation at December 31, 2006, results were extrapolated from the January 1, 2005 valuation. The next valuation of the accrued pension benefit obligation will be performed as at January 1, 2008.

Other information about the Corporation's Pension Plan and OPEB is as follows:

	2006		2005	
	Pension Plan	**OPEB**	Pension Plan	OPEB
Reconciliation and funded status				
Fair value of plan assets	**$ 12,323**	**$ –**	$ 11,693	$ –
Accrued benefit obligation	**12,658**	**1,234**	11,581	883
Funded status of plan – surplus (deficit)	**(335)**	**(1,234)**	112	(883)
Unamortized transitional (asset)/obligation	**(1,009)**	**137**	(1,135)	154
Unamortized net actuarial loss	**358**	**522**	641	329
Unamortized past service cost	**225**	**–**	242	–
Accrued liability, net of valuation allowance	**$ (761)**	**$ (575)**	$ (140)	$ (400)
Transfers to other plans and benefits paid	**$ 1,337**	**$ 18**	$ 918	$ 14
Employee contributions	**508**	**–**	372	–
Employer contributions	**58**	**18**	630	14
Pension expense	**678**	**194**	404	90

The total cash paid or payable in 2006 was $76 (2005 – $644).

Note 9 Contingencies, Commitments and Guarantees

In the normal course of business, the Corporation is party to a number of lawsuits, the outcome of which is not determinable at this time. However, in the opinion of management, these lawsuits should not result in material losses to the Corporation.

The Corporation has future minimum annual lease payments as follows:

	Premises Leases	Computer and Office Equipment Leases	Total Leases
2007	$ 725	$ 689	$ 1,414
2008	735	365	1,100
2009	735	31	766
2010	740	–	740
2011	721	–	721
2012 and thereafter	3,443	–	3,443
	$ 7,099	$ 1,085	$ 8,184

The Corporation has agreed to indemnify its directors and certain of its officers and employees against any liability incurred in their capacity as a director, officer or employee of the Corporation in accordance with the Corporation's by-laws. The nature of the indemnification undertakings precludes making a reasonable estimate of the maximum potential amount the Corporation could be required to pay to third parties, as the amounts are dependant upon the outcome of future contingent events, the nature and likelihood of which cannot be determined at this time. Historically, the Corporation has made no significant payments under such indemnification provisions.

Note 10 Fair Values of Financial Instruments

The fair values of investments are disclosed in Note 4. The carrying values of other financial instruments approximate their fair values.

Corporate Information

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Questions or comments regarding Tarion Warranty Corporation or any information appearing in the Annual Report may be directed to:

Tarion Warranty Corporation
Corporate Affairs Department
Telephone: 1-877-982-7466

The Corporation's Annual Report can also be found on the Tarion website at **www.tarion.com**.